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In the Supreme Court of the United States

OCTOBER TERM, 1944

No. 802

ESTATE OF ISAAC G. JOHNSON, PETITIONER

v.

THE UNITED STATES

ON PETITION FOR A WRIT OF CERTIORARI TO THE COURT OF CLAIMS

BRIEF FOR THE UNITED STATES IN OPPOSITION

OPINION BELOW

The opinion of the court below (R. 46–49) is reported in 57 F. Supp. 159.

JURISDICTION

The judgment of the Court of Claims was entered on October 2, 1944 (R. 49). The petition for a writ of certiorari was filed on December 30, 1944. The jurisdiction of this Court is invoked under Section 3 (b) of the Act of February 13, 1925, as amended by the Act of May 22, 1939.

QUESTION PRESENTED

Whether petitioner was "carrying on or doing business" within the meaning of Section 105 of the Revenue Act of 1935, as amended, and similar provisions of the Revenue Act of 1938 and of the Internal Revenue Code so as to be subject to the capital stock tax imposed thereby.

STATUTES AND REGULATIONS INVOLVED

The applicable portions of the statutes and regulations involved are set forth in the Appendix, *infra*, pp. 13–17.

STATEMENT

The special findings of fact of the Court of Claims (R. 29–45) may be summarized as follows:

Isaac G. Johnson died in 1899 leaving a considerable estate consisting of a large foundry and substantial real estate holdings at or near Spuyten Duyvil, New York City. Shortly after his death, a plan was submitted to his widow and children, who were entitled to the major part of his estate, under which the business interests of the decedent could be continued and a convenient means provided for the distribution of the estate upon its final liquidation to the various parties interested therein. Under that plan two corporations were to be organized, one to carry on the steel business, and the other the real estate business. Accordingly, the petitioner, a New York corporation, was organized in 1904 and acquired from the executors

and trustees of Johnson's estate real estate, consisting of approximately 20 acres; as consideration for the transfer, petitioner's capital stock was issued to the executors and trustees of Johnson's estate. The purposes of the petitioner, as stated in the certificate of incorporation, broadly included almost every phase of dealing in real estate, such as buying, selling, and renting of properties, dealing in stocks and bonds, and supervising, managing, and protecting the property. (R. 29–31.)

The widow of Isaac G. Johnson died in November 1906, and final accounting, settlement, and distribution of the assets of Johnson's estate were made by the surviving executor and trustee. The executor and trustee was finally discharged by decree of the surrogate court on November 30, 1906, and at that time the petitioner's stock which had been received by the executors and trustees, as above set forth, was distributed to the beneficiaries of the estate. (R. 32.)

Petitioner, however, continued its existence and between 1904 and 1925 made further acquisitions of real estate, some of which was improved property, and proceeded in various ways to develop and improve its properties, and engaged in extensive activities in connection therewith, and in the renting and selling thereof. But by about 1925, petitioner had practically ceased purchases of additional properties and by 1929 had reduced its

holdings, totaling approximately 95 acres, to about 47 acres. (R. 32–35.)

On November 4, 1929, the petitioner adopted a resolution stating that it was its policy gradually to liquidate its affairs and resolved that the sum of $150,000, from petitioner's paid in surplus, be distributed pro rata in liquidation among the holders of the stock of the corporation. This was accordingly done. In November 1938, a dividend of $5.25 a share was paid. (R. 35–36.)

During the period from about 1925 to 1929, petitioner discontinued many of its activities previously engaged in and reduced its operation to the maintenance and management of its remaining properties and the making of such sales as it deemed advantageous. It continued in that manner to and including the year 1936 as well as for sometime thereafter, maintaining an office with an accountant, two stenographers, and one or two outside ground keepers, receiving rents, making repairs, seeking legal advice, negotiating with promoters and architects, and considering and undertaking agency contracts and projects for the favorable marketing of its holdings. Substantially the same condition continued through the years 1937, 1938, and 1939. (R. 36.)

The real estate market was adversely affected by the depression which began in 1929 and continued unsettled until the outbreak of the war in Europe, after which there came an almost break-down of

the market for petitioner's property for private use. Petitioner's efforts during that time were directed towards the maintenance of a certain type of development in the area of its holdings which it considered for its best interests in the ultimate disposition thereof. Its president joined the Real Estate Board of the Bronx for the purpose of keeping in touch with real estate movements and to have access to records. He also joined the Home Owners' Association in that area to keep informed and to participate in efforts for or against zoning and other changes. During the years 1937, 1938, and 1939, petitioner did not make any sales to private parties. However, during that period it sold land to the City of New York, reducing its acreage from 45 acres in 1937 to approximately 37 acres. (R. 37–38.)

During the years 1937, 1938, and 1939, and for about the ten preceding years, petitioner engaged in activities which had for their purpose the ultimate disposition of its holdings at a profit without the undertaking of new activities which would interfere with or unduly retard an early advantageous disposition. While the properties were at all times for sale, at no time did petitioner offer them for sale at the best price which could be obtained but it gave consideration to whatever offers were received with the view of determining whether sales at the prices offered would be to its best interest. It continued to carry on with sub-

stantial taxes and operating expenses, with the hope that it might ultimately dispose of its properties on advantageous terms in an orderly liquidation. (R. 45.)

Petitioner filed capital stock tax returns for the fiscal years 1937, 1938, and 1939, claiming exemption on the ground that it was in process of liquidation and was not doing business within the meaning of the capital stock tax act. These claims for exemption were rejected by the Commissioner of Internal Revenue and after assessment the capital stock taxes for those years were paid. Thereafter claims for refund were filed and rejected.[1] (R. 42–45.)

The court below, upon the foregoing findings, held that petitioner was doing business during the fiscal years 1937, 1938, and 1939 and was subject to the capital stock tax (R. 46–49).

ARGUMENT

Capital stock taxes are imposed by Section 105 of the Revenue Act of 1935 as amended and

[1] The Government took the position in the court below that this suit could not be maintained for the recovery of the tax paid for the fiscal year ending June 30, 1937, since it was not brought within two years of March 17, 1939, the date when the Commissioner rejected the refund claim filed on September 7, 1938, and since the second claim, filed June 26, 1941, was not a timely and proper claim. In view of the decision on the merits in favor of the Government the court below did not decide this question. We are reserving this defense but do not believe it necessary to set forth the facts in connection therewith (R. 43–44) in this brief in opposition.

similar sections of the Revenue Act of 1938 and of the Internal Revenue Code (Appendix, *infra*, pp. 13–14) upon every corporation with respect to "carrying on or doing business." Article 43 (a) (5) of Treasury Regulations 64 (Appendix, *infra*, pp. 15–16) provides that, in general, doing business includes any activities of a corporation if it engages in—

> the orderly liquidation of property by negotiating sales from time to time as opportunity and judgment dictate and distribution of the proceeds as liquidation is effected—for example, the liquidation of an estate, or of properties taken over from another corporation, or of the shareholders' fractional interests in particular property.

The decision of the court below that the activities of the petitioner corporation constitute doing busines is clearly correct. "Engaged in activities which had for their purpose the ultimate disposition of its holdings at a profit" (R. 45), selling its properties as they could be advantageously disposed of, maintaining an office in connection therewith, receiving rents, making repairs, and performing other acts necessary and incidental to such activities, petitioner certainly falls within the terms of the above regulation which was specifically approved by this Court as a correct interpretation of the law in *Magruder* v. *Washington, B. & A. Realty Corp.*, 316 U. S. 69. In that case the taxpayer corporation was organized

with broad corporate powers by a bondholders' protective committee for the purpose of liquidating certain real properties. From the time of its incorporation it was carrying on negotiations for the sale of properties acquired, selling the same from time to time as satisfactory offers were received, and renting unsold properties in an attempt to earn the carrying charges pending ultimate disposition thereof. This Court held that the corporation came within the terms of the above-quoted section of the regulations which was valid, and that it was, therefore, subject to the capital stock tax.

Petitioner's contention that it is not subject to this tax rests upon the theory that it was a corporation organized to conduct a real estate business which it did for a number of years; that during 1929 it decided to liquidate that business and from then through the years in controversy was engaged in liquidation; and that it, therefore, comes within the provisions of Article 43 (b) (1) of the Regulations (Appendix, *infra*, pp. 16–17).[2]

[2] This Article provides that a corporation is not considered as "doing business" if its corporate powers are limited to the mere owning and holding of property or if it has retired from its regular business and has so reduced its activities. It further provides, however, that a corporation which has retired from its business is subject to the tax "if, nevertheless, it engages in other business activities or maintains its organization for the purpose of continued effort in the pursuit of profit or gain."

In this connection, petitioner asserts (Br. 28–32) that the cases in which corporations engaged in liquidation have been held taxable are those in which the corporation was doing the business for which it was organized. The Court of Claims, however, specifically found (R. 30) that petitioner was organized under a plan whereby a convenient means could be provided "for the distribution of the estate upon its final liquidation to the various parties interested therein." The fact that petitioner's articles of incorporation were very broad and included all phases of the real estate business is not material. Neither is the fact that its extensive activities in its earlier years included purchases of additional real estate. This could well have been a part of its program to liquidate the properties to the best financial advantage of the parties.

Moreover, Article 43 (b) (1) of the Regulations does not recognize any such test as the petitioner suggests, but provides that even if the corporation has retired from its principal business it is subject to the tax if it maintains its organization for the purpose of continued effort in the pursuit of profit or gain.[3]

This Court, in the *Washington, B. & A.* case, *supra,* pp. 72–73, recognized that Article 43 (b)

[3] In the 1936 edition of Regulations 64, referred to in the *Washington, B. & A.* case, *supra,* this provision appeared in Article 43 (b) (2).

(2) (Regulations 64, 1936 edition),[4] is not inconsistent with Article 43 (a)) (5) and was of the opinion that the activities of the corporation in that case fitted into the later Article and that it did not fall into that "state of quietude" covered by the specific language of Article 43 (b) (2). Even if petitioner was organized for purposes other than the liquidation of the estate of Isaac G. Johnson, as it contends, it was actively engaged in business during the years in question. Although its ultimate purpose may have been to liquidate, the properties were to be retained until petitioner obtained good prices. Petitioner was engaged in substantial activities in the pursuit of profit or gain (R. 38, 45). Cf. *Von Baumbach* v. *Sargent Land Co.*, 242 U. S. 503.

The decision of this Court in the *Washington, B. & A.* case, *supra,* has not been limited in its application to those cases where a corporation is organized for the purpose of liquidation but it has been held to cover cases where a corporation, organized for other purposes, has been in liquidation during the taxable years but has carried on activities in connection therewith sufficient to bring it within the scope of the regulations subjecting the corporation to the capital stock tax. *United States* v. *Western Shore Lumber Co.*, 136

[4] This article is similar to Article 43 (b) (1) of the 1938 edition of the Regulations.

F. 2d 628 (C. C. A. 9th); *National Commercial Title & Mortgage Guaranty Co.* v. *Duffy,* 132 F. 2d 86, 90–91 (C. C. A. 3d); cf. *San Fernando M. Land Co.* v. *Commissioner,* 135 F. 2d 547 (C. C. A. 9th).

The fact that in an earlier case involving the same parties the Court of Claims held that petitioner was not subject to the capital stock tax for the fiscal years 1934, 1935, and 1936 (*Johnson's Estate* v. *United States,* 37 F. Supp. 617) does not furnish any ground for certiorari. Petitioner does not contend that such decision is *res judicata,* no doubt because that doctrine is inapplicable under the circumstances. *State Farm Mutual Automobile Insurance Co.* v. *Duel,* decided February 12, 1945, p. 6, slip sheet opinion, No. 115, this Term; *Engineers' Club of Philadelphia* v. *United States,* 95 C. Cls. 42, certiorari denied, 316 U. S. 700, rehearing denied, 317 U. S. 705, and authorities cited; see Paul and Zimet, *Federal Tax Litigation—Selected Problems in Res Judicata* (1937) 32 Ill. L. Rev. 139, 153–154. In its earlier decision, which was prior to the *Washington, B. & A.* decision, the Court of Claims did not consider the effect of the applicable provisions of the regulations (R. 46) and so reached, we believe, an erroneous result. The present decision is in accord with the regulations and with the decision of this Court in the *Washington, B. & A.* case, *supra.*

CONCLUSION

No conflict has been shown. The decision of the court below is correct and the petition should be denied.

Respectfully submitted.

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